Nascent signs of Economic Revival
January 2020

Governments measures and Monetary easing by RBI expected to reverse the economic slowdown in 2020

The domestic economy may see a moderate improvement in GDP in the next fiscal, supported by Government measures. Muted manufacturing activity hit by slowdown in automobile sector led the slowdown in the GDP to hit 4.55% in Q2 2019-20, the lowest in last 26 quarters. Though, nascent signs of recovery in some of the economic indicators are visible like moderate rise in passenger air traffic, sales of passenger cars and improved manufacturing activity. December manufacturing PMI bought huge respite to the otherwise gloomy industrial activity (evident from the continuous contraction in eight core sectors and IIP). The economy may see reversal in slowdown and show moderate improvement on quarter-on-quarter growth in the third and fourth quarters supported by the policy initiatives taken by the government and RBI. The upcoming release of advance estimates of GDP by CSO may give a better picture to the full year GDP estimates, and we expect a GDP growth of 5% in the fiscal 2019-20.

Reforms carried out by the Government have restored banks to health, with the gross NPAs of PSBs declining from Rs. 8.96 lakh crore in March 2018 to Rs. 7.27 lakh crore in September 2019 and their provision coverage ratio rising to 76.6% in Sept 2019, their highest level in seven years. Moreover, 13 banks have reported profits in H1FY20. With improved asset quality and internal resource generation, PSBs are expected to support prudential credit growth in the near term. To ease the flow of credit and to improve the liquidity conditions of banks and NBFCs, the government has taken various measures recently. However, bank credit to industries in the fiscal so far remained negative at 3.9% as the transmission of monetary policy actions remained sluggish so far. The NBFC/HFC sector is showing signs of stability and are able to raise funds from market. Bank’s exposure to NBFCs increased 14% in the April to November 2019 period, but this could be largely due to better entities being able to obtain higher financing from banks. As against the cumulative reduction in the policy repo rate by 135 bps during February-October 2019, the 1-year median MCLR has declined by just 49 basis points. A large quantum of rate cuts has still not been transmitted, hence, the Monetary Policy Committee kept the policy repo rate unchanged at 5.15% in its December 2019 meeting, after five successive rate cuts. Going forward we expect, RBI will adopt a wait and watch approach amid mounting inflationary pressures as the risks from international oil prices has also increased.

The declining investment, stagnant exports and rising unemployment is clearly a wakeup call for the government to fast track the reform process and provide substantial stimulus for reviving growth momentum. The government has already proposed to spend Rs 13.6 lakh crore and Rs 19.5 lakh crore in the fiscal 2019-20 and 2020-21, respectively (as part of its Rs 102 lakh crore capital expenditure in infrastructure sectors during the fiscals 2020 to 2025), which is expected to boost the infrastructure activity significantly in the next fiscal. If structural reforms are undertaken, FY 2021 could have a growth of 5.5% to 6%.
MACRO-ECONOMIC INDICATORS

Economy Trends

Despite the policy initiatives taken by the government and RBI’s continued accommodative stance, the growth slowed to a six-year low in the first half of 2019, with both consumption and investment decelerating owing to weak income growth (especially rural) and stresses in the financial sector. On the external sector, after a rise in vulnerabilities in 2018, stability has returned in 2019, anchored by high foreign exchange reserves and a modest current account deficit.

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**Quarterly Growth in GDP and CAD as a ratio of GDP (%)**

<table>
<thead>
<tr>
<th>Quarter</th>
<th>GDP Growth</th>
<th>CAD (RHS)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mar-17</td>
<td>-0.4</td>
<td></td>
</tr>
<tr>
<td>Jun-17</td>
<td>-2.4</td>
<td></td>
</tr>
<tr>
<td>Sep-17</td>
<td>-1.1</td>
<td></td>
</tr>
<tr>
<td>Dec-17</td>
<td>-2.1</td>
<td></td>
</tr>
<tr>
<td>Mar-18</td>
<td>-1.8</td>
<td></td>
</tr>
<tr>
<td>Jun-18</td>
<td>-2.3</td>
<td></td>
</tr>
<tr>
<td>Sep-18</td>
<td>-2.9</td>
<td></td>
</tr>
<tr>
<td>Dec-18</td>
<td>-2.7</td>
<td></td>
</tr>
<tr>
<td>Mar-19</td>
<td>-2.0</td>
<td></td>
</tr>
<tr>
<td>Jun-19</td>
<td>-0.7</td>
<td></td>
</tr>
<tr>
<td>Sep-19</td>
<td>-0.9</td>
<td></td>
</tr>
</tbody>
</table>

*P: Projections, Source: MOSPI, BWR Research*

**Performance in Eight Core Industries and Index of Industrial Production (IIP)**

<table>
<thead>
<tr>
<th>Month</th>
<th>IIP (y-o-y growth in %)</th>
<th>Core Industries (y-o-y growth in %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Oct-18</td>
<td>4.4</td>
<td></td>
</tr>
<tr>
<td>Nov-18</td>
<td>4.9</td>
<td></td>
</tr>
<tr>
<td>Dec-18</td>
<td>5.4</td>
<td></td>
</tr>
<tr>
<td>Jan-19</td>
<td>5.9</td>
<td></td>
</tr>
<tr>
<td>Feb-19</td>
<td>6.4</td>
<td></td>
</tr>
<tr>
<td>Mar-19</td>
<td>6.9</td>
<td></td>
</tr>
<tr>
<td>Apr-19</td>
<td>7.4</td>
<td></td>
</tr>
<tr>
<td>May-19</td>
<td>7.9</td>
<td></td>
</tr>
<tr>
<td>Jun-19</td>
<td>8.4</td>
<td></td>
</tr>
<tr>
<td>Jul-19</td>
<td>8.9</td>
<td></td>
</tr>
<tr>
<td>Aug-19</td>
<td>9.4</td>
<td></td>
</tr>
<tr>
<td>Sep-19</td>
<td>9.9</td>
<td></td>
</tr>
<tr>
<td>Oct-19</td>
<td>10.0</td>
<td></td>
</tr>
<tr>
<td>Nov-19</td>
<td>-3.8</td>
<td>-1.5</td>
</tr>
</tbody>
</table>

*Source: MOSPI, eaindustry.nic.in, BWR Research*
Inflation and Monetary Policy Action

The Consumer Prices Index (CPI) increased significantly by 5.54%, touching a 40-month high in November 2019, due to 10% increase in food prices. Easing Core Inflation (excluding food and fuel) which remained at a moderate level of 3.5%, and deflation in fuel items owing to sustained fall in crude oil prices helped to keep the overall inflation within the band of 2 to 6%. Continued commitment to inflation targeting resulted in MPC taking a cautious stance in its December policy meeting and kept the policy rate unchanged at 5.15%.

Source: MOSPI, RBI, BWR Research

Crude Oil Prices and INR/USD rates

Crude oil prices steadily moving upwards since last two months posing potential risk for both inflation and the exchange rate. Huge foreign portfolio inflows and potential interventions by RBI helped the rupee to strengthen, despite rising oil prices.

Source: Ministry of Petroleum & Natural Gas, FBIL, BWR Research
### Merchandise Trade

Both exports and imports continued to decline in November 2019 compared to a year ago period, leading to 31% reduction in trade deficit (y-o-y). Trade deficit is lower primarily because imports have fallen at a faster rate than exports due to weak manufacturing activity and lower imports of raw materials and capital goods.

![India's Trade Balance](image)

Source: Ministry of Commerce, BWR Research

### Forex Reserves and Import Cover

Amidst the gloomy economic scenario, Foreign exchange reserves crossed $450 billion mark at the end of November 2019, reporting $57 billion increase in a year. The current level of forex reserves is adequate to cover 11.8 months of imports, which is comfortable and helps to absorb external shocks like exchange rate volatility. RBI is also seen intervening frequently in the current fiscal to manage rupee at a comfortable level.

![Forex Reserves and Import Cover](image)

Source: Ministry of Commerce, RBI, BWR Research

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**BWR Views**

External sector vulnerabilities eased in 2019 compared to 2018 going by the latest available data pointers like exports, exchange rate, CAD and forex reserves. The main external risks pertain to higher oil prices. With global economic slowdown, crude oil prices remained almost stable so far and helped to narrow domestic trade deficit. Any adverse international events which prompt increase in the prices of crude oil will aggravate India’s import bill, as India imports more than 70% of its oil needs. The killing of the powerful Iranian general, further escalated tensions in the Middle East, which is home to major oil producing countries and key energy supply routes.

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**BWR Views**

In the event of external pressures, India may continue to rely on exchange rate flexibility. With abundant forex reserves, RBI may intervene frequently to arrest any sharp fall.
**BWR Views**

The cut in corporate tax rates expected a shortfall of Rs 145,000 crore revenue to the Government. The recent disinvestments announcement by Government is likely to reduce its financial burden and improve public finances. The stake sales are equally critical to meet its disinvestment target of Rs 1.05 lakh crore set for the current fiscal year.

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**Government Accounts**

The fiscal deficit has crossed the Budget Estimates (BE) of Rs 7037.60 billion to Rs 8,078 billion during April to November 2019 period. Both total expenditure and total receipts increased by ~13% each over the comparable period last year. Through disinvestments, government has collected Rs 17,364 crore so far and expected to generate more to bridge the fiscal gap. Despite RBI’s dividend transfer, it has been expected that the fiscal deficit target is likely to be missed by 0.5 percentage points in the current fiscal.

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**Govt Accounts: Trends in Revenue and Expenditure (Rs Bn)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Receipts</th>
<th>Total Expenditure</th>
<th>Fiscal Deficit</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019-20 BE</td>
<td>20,826</td>
<td>7,038</td>
<td>-5,000</td>
</tr>
<tr>
<td>2018-19 (Apr-Nov)</td>
<td>16,132</td>
<td>7,166</td>
<td>-5,000</td>
</tr>
<tr>
<td>2019-20 (Apr-Nov)</td>
<td>18,201</td>
<td>8,078</td>
<td>-5,000</td>
</tr>
</tbody>
</table>

Source: Controller General of Accounts, Ministry of Finance, BWR Research

The gross GST revenue collected in the month of November and December 2019 crossed one lakh crore each, showing steady rise in collections. During April-December 2019 vis-à-vis 2018, the gross GST revenue collection has grown by 4.3% and the December 2019 GST collection is the third highest monthly collection since introduction of GST.

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**GST collection (Rs billion)**

Source: Ministry of Finance, BWR Research
SECTORAL INDICATORS

Automobiles

Domestic automobile sales fell by 12% y-o-y in the month of November 2019 largely driven by weak sales of commercial vehicles and two wheelers. Commercial vehicle sales were down by 15% and two & three wheelers sales were down by 14% y-o-y in November 2019. The weak commercial vehicle sales reflect the subdued state of industrial activity in the country and weak two wheeler sales indicate low rural demand. Commercial vehicles sales were also impacted by revised axle norms and financing issues due to NBFC crisis.

Though there was healthy growth in automobile sales in September and October on a sequential basis due to festive buying, this recovery was short lived and in November the sales again slipped in the red zone.

![Automobile Sales (Growth y-o-y)](image)

Source: CMIE, BWR Research

On the export front, there has been a growth of 18% in November 2019, which is a result of low base in November 2018, when the exports fell for the first time in last 21 months. Though, there has been a growth in overall export numbers in November 2019, commercial vehicles still registered a decline of 29% y-o-y in exports.

BWR Views

Commercial vehicle sales will continue to remain muted going forward. However, it might pick up in the last quarter of FY20 due to anticipated pre-buying by fleet owners before the BS-VI norm kicks in from April 2020. Though, the sales may still be lower than the previous year’s sales, but is expected to improve on month-on-month basis. Also, soon to be announced, scrappage policy might provide some support to the automobile sales recovery.
Telecom

Consolidation of the market continues with Jio increasing its market share and driving the overall subscriber additions in the sector. The increase in subscriber base is likely driven by rise in rural subscribers. The subscriber base is expected to widen further as the penetration increases, especially in rural areas. Cheap data and feature phones will drive the subscriber base in rural areas.

Source: TRAI, BWR Research

All the telecom operators hiked their tariffs in the month of December 2019 between the range of 30%-40% in order to improve profitability. While, the move will certainly help in bringing down the losses of incumbents, the troubles for the sector are far from over as the petition filed by the incumbents in the Supreme Court regarding AGR dues is still pending. Also, tariff hikes will not serve the desired purpose unless it is accompanied by a reduction in the license fee and spectrum usage charges for which there are no indications from the Government. With the telcos already under immense liquidity pressure, the impending 5G auction is also expected to get a lukewarm response.
Power

Power generation fell by 13% y-o-y in October 2019 reflecting a slump in demand particularly from industrial in the country. This is evident from lower generation from thermal sources, as the thermal power units continue to struggle on account of falling demand amid reduction in manufacturing and industry output. The power sector also faces other challenges such as non-availability of adequate bank credit, absence of long term Power Purchase Agreements (PPAs) and issues related to coal tie-ups.

Despite taking various measures, the Government has not been able to fully resolve the issues associated with the power sector. The Finance Minister, in her recent announcements related to infrastructure sector push, has highlighted projects worth Rs. 25 trillion being in the pipeline for energy sector. Also, various other reforms for upgrading technology and improving operational efficiency of power utilities are expected to be rolled out soon. With majority of Discoms still continuously failing to honour their commitments, how new reforms will be able to improve the situation is yet to be seen.

Source: Central Electricity Authority, BWR Research

India's power supply position improved in October 2019. However, the country is still not power surplus due to DISCOMS stressed financials on account of its mounting losses and huge debt burden.

Source: Central Electricity Authority, BWR Research
Steel

The ongoing stress in the automobile and real estate sectors curtailed the demand for steel. Global issues continue to weigh on prices, however domestically demand is expected to pick up, going by the recent announcement about a substantial push to infrastructure by the Finance Minister. As per the announcement, Rs. 102 lakh crores are expected to be invested for infrastructure over the next five years, with 22% coming from the private sector and 39% each from the Central and State governments.

Cement

Cement prices have started correcting from June 2019, after witnessing a sharp increase in April and May 2019, which was based on anticipation of healthy demand going forward. The prices started coming down reflecting a weak actual demand.
BWR Views

The industrial sector, which has relatively higher levels of non-performing assets (NPAs), witnessed 3.9% fall in credit deployment in the current fiscal so far. Credit growth is expected to remain muted in the coming months on account of slowdown in private investments in the economy.

Banking

Overall bank credit during the period April-November 2019, increased by only 0.5% as compared with a growth of 5.3% during the same period previous year. The slowdown was more evident in the industry and services sector. This can be attributed to cautious lending approach by banks as they have shifted focus towards lending to the retail sector, where the probability of delinquency is lower. Also, with the slowdown in the economy, the demand for credit has dried up with low or almost no private investments happening in the economy.

Airline

Domestic passengers carried by airlines increased by 11% y-o-y in the month of November 2019, highest growth in the year 2019. This growth was aided by low fares and the onset of year-end holiday season.

Source: DGCA, BWR Research

BWR Views

Air Passenger traffic growth is expected to be healthy in December as well. However, domestic air passenger traffic is expected to grow in the single digits this fiscal, mainly because of weak growth in the beginning of the years due to capacity shortage caused by grounding of Jet Airways.

Source: DGCA, BWR Research
**DEBT MARKET INDICATORS**

**Movements in Bond Yields**

Bond yields (annualised) of Public Sector Units (PSUs), Corporates and Non-Banking Finance Companies (NBFCs) maturing in 5-year, 3-year and 1-year tenure with corresponding Government Securities and Marginal Cost of funds based Lending Rate (MCLR) of banks are provided below.

![5-year AAA Corporate Bond yields vs Gsec yield, MCLR](image1)

![3-year AAA Corporate Bond yields vs Gsec yield, MCLR](image2)

Source: FIMMDA, SBI, HDFC, BWR Research

**BWR Views**

Going forward, we expect the yields to continue to remain volatile on account of uncertainty on next repo rate cut by Reserve Bank of India amid higher crude oil prices on back of geopolitical tensions.
The yields of AAA rated corporate bonds maturing in 5-year, 3-year and 1-year have little changed in December compared to easing trend seen in November due to pause in rate cut cycle amid uncertainty in gauging further course of rate action by Reserve Bank of India’s Monetary Policy Committee on account of rising inflation.

Yield curve of AAA PSUs, NBFCs, Corporates and G-sec

The G-sec yield maturing in 1 year compared with Corporate bonds yields of PSUs, NBFCs and Corporates of similar maturity buckets have been volatile in the month of December due to unexpected pause in RBI's December monetary policy. However, the market is awaiting measures for revival in sentiments.
External Commercial Borrowings

Indian companies continue to prefer overseas borrowings on account of easy availability of longer tenure loans from overseas. In November 2019, companies’ borrowings through ECB increased 2.34% compared to same period previous year. However, on month-on-month basis in November ECBs reported slight fall due to some volatility in rupee and geopolitical tensions.

Source: RBI, BWR Research
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